



Special Report

A Few Reminders about the New AOMR

AOMR Update

by Mark Rowley

You have probably heard by now that Florida and a few other states have passed the new AOMR effective for 2003 yearend work. (We understand that the other states are Indiana, New Mexico, and Virginia). As we have reported before, this impacts many small companies (any company licensed in Florida or one of these other states) since they will have to do an asset adequacy analysis instead of a Section 7 opinion. See pages 3 and 4 of this newsletter for details on how states are dealing with this.

But the new AOMR also impacts any company which does asset adequacy analysis since some of the details of the required memorandum have changed. We had hoped that the impact of the new AOMR would be a good one in helping companies deal with state variations in valuation laws, but this part of the AOMR model doesn't seem to be getting adopted.

The new requirements involve enhanced documentation of

assumptions in the memorandum and a brand new requirement called "the Regulatory Asset Adequacy Issues Summary". We recommend that the entire regulation be reviewed, as there are a few other places where wording has changed to achieve clarification.

References in this article are to Florida's version of the regulation. This can be found by following these instructions:

Florida Administrative Code rule 4-138, part III, is available on the internet at:

- I. <http://fac.dos.state.fl.us>
- II. Click Chapter 4 – Department of Insurance – <http://fac.dos.state.fl.us/faconline/chapter04.pdf>
- III. Click D4 – 138.040 to get to the beginning of Part III Actuarial Opinion & Memorandum Regulation.

Enhanced Documentation of Asset and Liability Assumptions

For reserve (liability) assumptions, there are two new requirements:

- 1) Identification of any explicit or implicit guarantees made by the general account in support of benefits provided through a separate account or under a separate account policy or contract and the methods used by the appointed actuary to provide for the guarantees in the asset adequacy analysis.

- 2) Documentation of assumptions to test reserves including lapse rates, interest crediting rate strategy, mortality, policyholder dividend strategy, competitor or market interest rate, annuitization rates, commissions and expenses, and morbidity.

For assets, the following assumptions need to be documented – Default costs, bond call functions, mortgage prepayment function, determining market value for assets sold due to disinvestment, and determining yield on assets acquired through the investment strategy.

For both asset and liability assumptions, the documentation of the assumptions shall be such that an actuary reviewing the actuarial memorandum could form a conclusion as to the reasonableness of the assumptions.

See page two for information on the Regulatory Asset Adequacy Issues Summary.

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The Van Elsen Report

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Regulatory Asset Adequacy Issues Summary

Rather than try to summarize what this is about, it is more helpful to quote it verbatim:

- (a) The regulatory asset adequacy issues summary shall include:
1. Descriptions of the scenarios tested (including whether those scenarios are stochastic or deterministic) and the sensitivity testing done relative to those scenarios.
 - a. If negative ending surplus results under certain tests in the aggregate, the actuary should describe those tests and the amount of additional reserve as of the valuation date which, if held, would eliminate the negative aggregate surplus values.
 - b. Ending surplus values shall be determined by either extending the projection period until the in force and associated assets and liabilities at the end of the projection period are immaterial or by adjusting the surplus amount at the end of the projection period by an amount that appropriately estimates the value that can reasonably be expected to arise from the assets and liabilities remaining in force.
 2. The extent to which the appointed actuary uses assumptions in the asset adequacy analysis that are materially different than the assumptions used in the the previous asset adequacy analysis.
 3. The amount of reserves and the identity of the product lines that had been subjected to asset adequacy analysis in the prior opinion but were not subject to analysis for the current opinion.
 4. Comments on any interim results that may be of significant concern to the appointed actuary.
 5. The methods used by the actuary to recognize the impact of reinsurance on the company's cash flows, including both assets and liabilities, under each of the scenarios tested; and
 6. Whether the actuary has been satisfied that all options whether explicit or embedded, in any asset or liability (including but not limited to those affecting cash flows embedded in fixed income securities) and equity-like features in any investments have been appropriately considered in the asset adequacy analysis.
- (b) The regulatory asset adequacy issues summary shall contain the name of the company for which the regulatory asset adequacy issues summary is being supplied and shall be signed and dated by the appointed actuary rendering the actuarial opinion.

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AOMR Survey

We surveyed the states to determine where they stood on AOMR.

21 states have responded and this is the breakdown:

4 are effective in 2003 - FL, IN, NM, VA.

3 are effective in 2004 - CO, IA, ND.

5 plan to be effective in 2004 - AK, CA, ME, TX, WV.

2 plan to be effective in 2005 or later - LA, NY.

7 are reviewing AOMR but have no plans to adopt - IL, KS, MI, MN, MS, UT, WI.

Alaska - Has not adopted the regulation, but intends to adopt the regulation sometime in 2004.

California - Is in the process of adopting the revised Actuarial Opinion and Memorandum Regulation, with an expected effective date of December 31, 2004. The California version is not exactly the same as the one adopted by the NAIC.

Colorado - Has adopted the new AOMR. It is our revised regulation 3-1-8 (available on our website, www.dora.state.co.us/insurance), and is effective January 1, 2004. We stayed with the model for the most part - as I recall, we don't have as many options available for obtaining permission to use an alternate opinion. We also are requiring our domestic companies to do at least the standard 7 interest scenarios.

Florida - Has adopted the new AOMR. Effective January 23, 2003.

Illinois - Has not adopted the AOMR and are in the process of reviewing it.

Indiana - Rule 57, Actuarial Opinion and Memorandum, effective December 31, 2003. All life insurance companies and fraternal benefit societies doing business in Indiana shall submit a statement of opinion on the adequacy of the reserves and related actuarial items based on an asset adequacy analysis and a memorandum in support thereof in accordance with this Rule.

Iowa - Has adopted the regulation effective January 1, 2004.

Kansas - Has not yet adopted the new AMOR. We are in the process of reviewing it and determining what impact it has on the codification regulations (i.e. what impact it will have on the Accounting Practices and Procedures Manual).

Louisiana - Plans to promulgate the new AOMR this year. Will likely make it effective January 1, 2005. Plan to make sufficient revisions to allow us to make special concessions for our single state domestics.

Maine - Is considering adopting it later this year.

Michigan - Has not adopted the new AOMR. They are still reviewing and discussing adopting the new AOMR. At this time, they are leaning toward adopting.

Minnesota - Has not adopted the amendments and does not have plans to do so at this time.

Mississippi - Is considering this regulation but at this time we do not have any plans to adopt it in the immediate future.

New Mexico - Adopted the current NAIC model for AOMR effective October 1, 2003. The model was adopted as 13.2.6 NMAC and does not materially differ from the model. The new AOMR requirements are applicable to 2003 Annual Statement filings and their supporting documents.

New York - Has not yet adopted the new AOMR. They plan to adopt the new AOMR with an effective date of December 31, 2005 or 2006. They plan on making various changes primarily regarding additional required information which the Department believes is essential for monitoring asset adequacy. They have already started the drafting process for incorporating the revisions made by the NAIC.

North Dakota - Adopted the Model for AOMR by Administrative Rule, and it is effective March 1, 2004.

Texas - Has not yet adopted the new AOMR but is currently working to propose the new AOMR in our adoption process where staff will propose an effective date in 2004 to be applicable for 2004 year-end actuarial opinions.

Utah - Has not adopted the new AOMR. No decision has been made at this point whether to adopt AOMR. We have few domestic companies, and most of them currently qualify for an exemption from asset adequacy testing. The exemptions has been eliminated from the AP&P Manual which therefore requires that these companies either perform asset adequacy testing or disclose effects of not doing so. We need to evaluate the impact of the change on our domestic companies.

Virginia - Adopted the new AOMR effective for 2003 yearend work.

West Virginia - Has not adopted the new AOMR, however we are expecting to next year or so.

Wisconsin - Has not adopted the new AOMR, but we have begun the process that might eventually result in passage of the new rule. Their legal unit has issued a notice of scope, which essentially notifies the public that we will be considering a rule change. They are still completing the draft of the proposed new rule. I They anticipate that it will be substantially the same as the model regulation. They do not know the effective date at this time.

Van Elsen Consulting, Inc.

Van Elsen Consulting, Inc. is an actuarial consulting firm. **James N. Van Elsen, FSA, MAAA, CPA, FLMI** is president and responsible for the work completed. We specialize in serving the needs of smaller life insurance companies.

As you consider your actuarial consulting needs in the future, consider the firm that works hard to reduce the cost of regulation for its clients.

Areas of Recent Assignments:

- ✓ Asset Adequacy Analysis for small to medium sized companies
- ✓ Illustration Regulation Opinions
- ✓ Product Development
 - Term Insurance Using 2001 CSO
 - Simplified Issue Products
 - Return of Premium Term Products
 - Universal Life Products
 - Preneed Products
 - Final Expense Products
 - LTC Riders
- ✓ Reserve Peer Reviews
- ✓ Review of "XXX" X-Factors, Significantly Reducing Initial Reserve Strain
- ✓ Assistance with Reinsurance Negotiations
- ✓ Individual & Group Major Medical Rating Assistance

Call Van Elsen Consulting, Inc.!!!

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